



0000067230

## BEFORE THE ARIZONA CORPORATION COMMISSION

0528

**COMMISSIONERS**

Jeff Hatch-Miller, Chairman  
William A. Mundell  
Mike Gleason  
Kristin K. Mayes  
Gary Pierce

2007 FEB 23 P 3:43

AZ CORP COMMISSION  
DOCUMENT CONTROLArizona Corporation Commission  
**DOCKETED**

FEB 23 2007

DOCKETED BY

Docket No. W-00000C-06-0149

IN THE MATTER OF THE COMMISSION'S  
GENERIC EVALUATION OF THE  
REGULATORY IMPACT FROM THE USE OF  
NON-TRADITIONAL FINANCING  
ARRANGEMENTS BY WATER UTILITIES AND  
THEIR AFFILIATES

**REPLY BRIEF**

Santa Cruz Water Company, LLC; Palo Verde Utilities Company, LLC; Global Water – Santa Cruz Water Company; Global Water – Palo Verde Utilities Company; Cave Creek Water Company; and Hassayampa Utility Company (the “Global Utilities”) and Global Water Resources, LLC (“Global Parent”)(collectively “Global”) hereby provide their reply to the Brief filed by Staff on February 9, 2007 in this docket.

**I. Preliminary Statement.**

Global agrees with much of what Staff said in its brief. In particular, Staff properly noted that Infrastructure Coordination and Financing Agreements (“ICFAs”) serve many goals – such as water conservation and consolidation of weak utilities – that serve the public interest. Further, Staff was correct to conclude that this is not the right time to decide jurisdictional questions regarding Global Parent and other unregulated Global affiliates (collectively, the “Unregulated Affiliates”). Staff was also right to observe that piercing the corporate veil is very difficult.

Global agrees with Staff that, given the undeveloped state of the record, this is not the right time to reach firm conclusions or final decisions on jurisdictional or other questions. However, to the extent that the Commission desires to address these issues at this time, there are no grounds to find that any of the Unregulated Affiliates are public service corporations. First, only entities that

1 provide the services specified in the Arizona Constitution may be determined to be public service  
2 corporations. The Unregulated Affiliates do not provide water, wastewater, or any of the other  
3 specified services. Second, there are no grounds in the record for a finding of undercapitalization,  
4 fraud, or misconduct, and thus the separate corporate existence of the Unregulated Affiliates may  
5 not be disregarded. Third, so called “*Serv-Yu*” factors<sup>1</sup> do not support a finding that the Global  
6 Parent are public service corporations because they only provide non-utility service under private  
7 contract, with all utility services provided by the fully regulated Global Utilities. Thus, the time is  
8 not right to decide these issues, but if a decision is made now, there are no grounds for declaring  
9 the Unregulated Affiliates to be public service corporations.

10 **II. It is not prudent to make a decision at this time.**

11 Staff’s Brief repeatedly notes the limited state of the record at this time. For example, Staff  
12 noted that the jurisdiction issue “is not clear at this point.”<sup>2</sup> Likewise, Staff noted that “absent a  
13 more developed record... it is impossible to determine at this point with certainty” whether the  
14 Commission should take jurisdiction.<sup>3</sup>

15 Likewise, the Staff Report in the Generic Financing Docket<sup>4</sup> did not make any firm  
16 conclusions regarding ICFAs. Staff described its report as only a “preliminary evaluation”<sup>5</sup> and its  
17 suggestions as only “preliminary positions”<sup>6</sup> Further, the Director of the Utilities Division, Mr.  
18 Johnson, recently referred to the Staff Report as a mere “position paper” and encouraged the  
19 Commission to obtain further information.<sup>7</sup> Thus, it is clear that Staff’s analysis of the ICFAs is  
20 only tentative at this point.

21  
22  
23 <sup>1</sup> See *Natural Gas Service Co. v. Serv-Yu Co-Op.*, 70 Ariz. 235, 237-38, 219 P.2d 324, 325-36 (1950).

24 <sup>2</sup> Staff Brief at 2.

25 <sup>3</sup> Staff Brief at 10-11.

26 <sup>4</sup> Docket No. W-00000C-06-0149.

27 <sup>5</sup> Generic Financing Docket, Staff Report at 2.

<sup>6</sup> Generic Financing Docket, Staff Report at 4.

<sup>7</sup> Comments made during the Commission’s Staff Meeting on January 17, 2007.

1 It would not be prudent to base a final decision on incomplete, tentative analysis by Staff.  
2 Further, it is clear that the record will become much more developed in the future. It is our  
3 understanding that once this briefing schedule is complete, the Commission will request further  
4 rounds of comments in the Generic Financing Docket. In addition, there may be workshops or  
5 other information gathering sessions. Thus, the record will likely be further developed in the  
6 future. Therefore, Staff was correct to reserve judgment until all the facts are in. The Commission  
7 should follow the same course.

8 In addition, it should be noted that the Staff did not make a clear finding that ICFA fees  
9 should be treated as advances or contributions. As described above, Staff's conclusions were only  
10 tentative. Moreover, the relevant section of the Staff Report did not directly examine the ICFA's.  
11 Rather, this section analyzed a hypothetical only loosely based on the ICFA's.<sup>1</sup> This hypothetical,  
12 called "Scenario 3" differs from ICFA's in several important respects. For example, Scenario 3  
13 involves "services typically covered by 'off-site hook-up fees'". Our Comments in the Generic  
14 Financing Docket explained why the ICFA fees are substantially different from hook-up fees.

15 There are many other differences between ICFA fees and advances or contributions. For  
16 example, Global Parent pays taxes on the ICFA fees, while advances and contributions to water  
17 and wastewater companies are tax-free. In addition, ICFA fees only cover an approximation of the  
18 carrying costs of the plant – they do not directly pay for the plant, as suggested in Scenario 3.  
19 Moreover, ICFA fees are often used to pay for the acquisition and consolidation of small utilities,  
20 which does not impact rate base at all. Staff also notes that over-reliance on advances and  
21 contributions leads to undercapitalization and financially weak utilities.<sup>2</sup> It thus makes little sense  
22 to treat new alternatives to advances and contributions as being advances and contributions.

23 Most importantly, hook-up fees, and other financing methods that result in advances or  
24 contributions, simply do not result in regionally sized, conservation-focused infrastructure, such as  
25

26 \_\_\_\_\_  
27 <sup>1</sup> Generic Financing Docket, Staff Report at 5-6

<sup>2</sup> Generic Financing Docket, Staff Report at 6.

1 reclaimed water facilities, use of surface water, and construction of recharge wells. Such facilities  
2 are enormously capital intensive. It is therefore necessary for there to be a mechanism for  
3 investors to recover the carrying costs of these massive investments until they go into service.

4 Further, traditional methods do not result in consolidation of utilities. Tellingly, American  
5 Water (parent of Arizona-American) aims for between 20 and 30 acquisitions per year – yet it has  
6 not acquired any utility in Arizona in years.<sup>1</sup> Other publicly traded water companies also pursue  
7 acquisitions, but they avoid Arizona because Arizona’s traditional financing methods simply don’t  
8 support consolidation. Yet with more than 400 water companies and explosive growth in the state,  
9 there is a desperate need for such consolidation. The ICFA presents a new alternative that can  
10 partially fund consolidation activity. The Commission should not squash such a promising new  
11 alternative. And to be clear, Global does not claim exclusive rights to the ICFA model. Indeed,  
12 Global encourages other sophisticated companies with access to capital to adopt this method and  
13 provide the necessary capital to consolidate Arizona’s small, fragmented utilities and to build the  
14 massive amounts of conservation-based infrastructure that will be needed to sustain growth – the  
15 engine of our state’s economy.

16 Thus, ICFAs are clearly in the public interest. Staff correctly concluded that “ICFA type  
17 arrangements can provide appropriate long-term solutions which promote conservation of water  
18 supplies and efficient wastewater utilization.”<sup>2</sup> Staff was thus right to conclude that ICFA type  
19 agreements should be reviewed “on a case by case basis.”<sup>3</sup> Given the undeveloped state of the  
20 record, and the clear benefits of ICFAs, it is not prudent at this time to make blanket  
21 determinations regarding whether ICFA fees should be advances, or whether ICFA signatories are  
22 public service corporations.

23  
24  
25  
26 <sup>1</sup> “Water for Profit”, [www.cfo.com](http://www.cfo.com), dated February 1, 2007.

27 <sup>2</sup> Generic Financing Docket, Staff Report at 7.

<sup>3</sup> *Id.*

1     **III.     The Unregulated Affiliates are not public service corporations.**

2             For the reasons described above, this is not the time to decide these questions. But if the  
3 Commission wishes to push ahead with a decision at this time, there are no grounds to find the  
4 Unregulated Affiliates to be public service corporations. First and foremost, the Unregulated  
5 Affiliates simply do not provide water, wastewater, or any other service listed in the Article XV §  
6 2 of the Arizona Constitution. There is simply no reference in Article XV to coordination or  
7 financing services. Staff appropriately quotes the language of the key case: “we simply note that  
8 the constitutional definition is to be strictly construed and that [the holding company] itself does  
9 not provide any public service listed in the definition.” *Arizona Public Service Co. v. Arizona*  
10 *Corp. Comm’n*, 155 Ariz. 263, 267, 746 P.2d 4, 8 (App. 1987) *affirmed in relevant part, vacated*  
11 *in part on other grounds*, 157 Ariz. 532, 760 P.2d 532 (1988). A corporation which does not  
12 provide the listed services cannot be a public service corporation – that is simply the end of the  
13 matter. The text of the constitution permits no other result.

14             This conclusion is reinforced by the most recent case concerning public service  
15 corporations. Only months ago, the Court of Appeals noted that “[d]etermining whether an entity  
16 is a public service corporation requires a two-step process. First, we considered whether the entity  
17 satisfies the literal and textual definition of a public service corporation under Article 15, Section 2  
18 of the Arizona Constitution.” *Southwest Transmission Co-op. v. Arizona Corp. Comm’n*, 213  
19 Ariz. 427, 142 P.3d 1240, 1243 ¶ 16 (App. 2006) *citing Southwest Gas Corp. v. Arizona Corp.*  
20 *Comm’n*, 169 Ariz. 279, 285-86, 818 P.2d 714, 720-21 (App. 1991). If – and only if – step one  
21 produces an affirmative result, can the decision-maker move on to step 2 (the so-called “*Serv-Yu*”)  
22 factors. *See id.* No party contends that the Unregulated Affiliates meet the “literal and textual  
23 definition”, so the Unregulated Affiliates cannot be public service corporations.

24             Staff suggests that the Commission could engage in an “alter ego” or “veil piercing” type  
25 of analysis. However, as noted above, if an entity does not meet the “literal and textual definition”  
26 it cannot be considered a public service corporation. But in any event, Staff correctly notes that it  
27 is very difficult to pierce the corporate veil, explaining that “absent some fraud or injustice, Courts

1 are hesitant to simply ignore the corporate separation.”<sup>1</sup> The case most directly on point is *Arizona*  
2 *Public Service, supra*. That case involved the holding company of APS. The Commission argued  
3 that the court should disregard the separate corporate existence of the holding company. The court  
4 rejected that argument, noting that “[w]e decline to “pierce the corporate veil” because both [the  
5 holding company] and APS have maintained their separate corporate identities and because the  
6 Commission has offered no evidenced of undercapitalization, fraud, misconduct, or impropriety in  
7 the management or operation of the two companies.” *Arizona Public Service*, 155 Ariz. at 267,  
8 746 P.2d at 8. The Unregulated Affiliates have maintained their formal, separate identities, the  
9 regulated Global Utilities are highly capitalized, and no party has clearly identified any “fraud or  
10 injustice.” Thus, Staff correctly concludes that “absent a more developed record on such injustices  
11 or misconduct, it is impossible to determine at this point with certainty whether piercing of the  
12 corporate veil is appropriate.”<sup>2</sup>

13 In addition, the Commission “is without jurisdiction to compel” an entity to “submit to its  
14 control” when the entity has not been previously regulated and does not consent to the  
15 Commission making the jurisdictional finding. *See Williams v. Arizona Corp. Comm’n*, 102 Ariz.  
16 382, 430 P.2d 144 (1967). Instead, such determinations must be made in the courts.

17 **IV. The Serv-Yu factors do not support finding of jurisdiction.**

18 As noted above, the *Serv-Yu* factors do not apply because the Unregulated Affiliates do not  
19 meet the “literal and textual” definition in Article XV § 2. In addition, the Commission lacks  
20 jurisdiction to decide the issue under *Williams*. However, because Staff addressed the *Serv-Yu*  
21 factors, we will briefly address each factor. Staff only addressed Global Parent, so this discussion  
22 will involve only Global Parent.

23  
24  
25  
26  
27 <sup>1</sup> Staff Brief at 7.

<sup>2</sup> *Id.* at 10-11.

1           **A.     Factor One.**

2           The first factor is “what the corporation actually does”. Global Parent provides  
3 coordination and financing services under the ICFAs. It also consolidates regulated utilities and  
4 invests equity to fund infrastructure needs, including needed conservation infrastructure for  
5 reclaimed water, surface water, and recharged water. Global Parent does not provide water,  
6 wastewater or reclaimed water service. The ICFAs carefully limit the role of Global Parent to non-  
7 regulated functions. The regulated Global Utilities provide the water, wastewater, and reclaimed  
8 water services. No water, wastewater, or reclaimed water customer will ever receive a bill from or  
9 payable to Global Parent. The regulated Global Utilities remain subject to the CC&N process and  
10 resulting conditions. Further, they enter into main extension agreements for on-site facilities in  
11 accordance with Commission rules. Thus, this factor points against jurisdiction over Global  
12 Parent.

13           **B.     Factor Two.**

14           The second factor is dedication to public use. To meet this factor, the entity “must at least  
15 have undertaken to actually engage in business and supply at least some of his commodity to some  
16 of the public.”<sup>1</sup> Here, Global Parent does not supply the relevant commodity – water. And Global  
17 Parent does not deal with the general public – only developers and other large landowners. Thus,  
18 this factor points against a finding of jurisdiction.

19           **C.     Factor Three.**

20           The third factor is “articles of incorporation”. No provision in Global Parent’s articles  
21 suggests that it is a public service corporation.

22           **D.     Factor Four.**

23           The fourth factor is dealing with the service of a commodity in which the public has been  
24 generally held to have an interest. Again, Global Parent does not deliver a drop of water. Only the  
25 regulated utilities provide this service. Unlike *Southwest Transmission*, here Global Parent never  
26

---

27           <sup>1</sup> Staff Brief at 9 citing *Serv-Yu*.

1 takes ownership or possession of the relevant commodity. Thus, this factor points against a  
2 finding of jurisdiction.

3 **E. Factor Five.**

4 The fifth factor is “monopolizing or intending to monopolize the territory with a public  
5 service commodity.” *Serv-Yu*, 70 Ariz. at 238, 219 P.2d at 326. Again, Global Parent does not  
6 provide a public service commodity. And there is no intent to monopolize. A monopoly is only  
7 created – for the regulated utility – when the Commission grants a CC&N. The ICFAs expressly  
8 provide that if the Commission denies the CC&N, the landowner is free to terminate the ICFA.  
9 Thus, this factor also points against jurisdiction.

10 **F. Factor Six.**

11 The sixth factor is acceptance of “substantially all requests for service.” Here, Global  
12 Parent does not provide water, wastewater, or reclaimed water service. And even if the ICFAs are  
13 considered a relevant service, there is no evidence in the record that Global Parent accepts all  
14 requests for ICFAs. Thus, this factor points against jurisdiction.

15 **G. Factor Seven.**

16 Service under private contract points against jurisdiction, although this factor is not  
17 controlling. Again, Global Parent does not provide the relevant service. And in any event, the  
18 services it does provide are provided pursuant to private contracts (the ICFAs), so this factor  
19 points against jurisdiction.

20 **H. Factor Eight.**

21 The eighth and last factor is competition with other public service corporations. Staff notes  
22 that the “Coordinator and its operating affiliate[s] would together meet this criteria.”<sup>1</sup> But because  
23 there are no grounds to pierce the corporate veil, the companies must be analyzed separately.  
24 Global Parent does not compete directly with regulated utilities, although its regulated  
25  
26

---

27 <sup>1</sup> Staff Brief at 12.

1 subsidiaries, the Global Utilities certainly do. Because these are separate entities, this factor points  
2 against jurisdiction.

3 **I. Conclusion**

4 No factor points in favor of jurisdiction, so a public service corporation finding is clearly  
5 not warranted under the *Serv-Yu* factors, even if those factors could be applied in these  
6 circumstances.

7 **V. Jurisdiction over agreements.**

8 Staff also suggests that even if the Global Parent are not public service corporations, the  
9 Commission can still assert jurisdiction over the ICFAs. It is not clear what Staff means by this  
10 suggestion. They cite to *Woods*, the case that affirmed the Commission's Affiliated Interest Rules,  
11 A.A.C. R14-2-801 et seq. Santa Cruz Water Company recently became a "Class A" utility, so  
12 Global Parent is now subject to these rules. However, Staff does not point to any provision of  
13 those rules that apply here, and there does not appear to be any provision in the rules that apply to  
14 the ICFAs. The rules do require approval for agreements where the utility guarantees the obligations  
15 of an affiliate. A.A.C. R14-2-804(A)(1). The ICFAs involve no such guarantee – instead they  
16 involve the opposite – as Global Parent guarantees the obligations of the regulated utilities. It  
17 seems likely that the Commission would want to encourage parent companies to stand behind  
18 utilities in this way.

19 Staff may have been referring to its recommendation in the Staff Report that ICFAs be  
20 evaluated on a "case by case" basis in appropriate proceedings. Global fully agrees with that  
21 suggestion. The Commission certainly has the power to investigate the effect of ICFAs on rates in  
22 the context of a rate case. A rate case proceeding would supply a lot of the information that is  
23 missing from this record. And because the Commission clearly has jurisdiction over the rates of  
24 the Global Utilities, such an approach would provide a much firmer basis for the Commission to  
25  
26  
27

act. Global recently suggested that the Commission order several of the Global Utilities to file rate cases.<sup>1</sup>


**VI. Conclusion.**

Given the limited development of the record at this point, this is not the right time to decide the jurisdiction question. But if a decision is made, the Unregulated Affiliates are not public service corporations for several reasons – they do not meet the textual definition, there are no grounds for piercing the corporate veil, the *Serv-Yu* factors (even if applicable) do not support jurisdiction, and an any event, under *Williams*, the Commission may not assert jurisdiction under these circumstances.

Thus, the Commission should not make a jurisdictional finding at this time. The Commission would be on much firmer footing in evaluating the effects of ICFAs on rates in future rate cases for Global Utilities.

RESPECTFULLY SUBMITTED this 23<sup>rd</sup> day of February 2007.

Roshka DeWulf & Patten, PLC

By   
Timothy J. Sabo  
Michael W. Patten  
One Arizona Center  
400 East Van Buren Street, Suite 800  
Phoenix, Arizona 85004

Attorneys for Global Water Resource

Original + 13 copies of the foregoing  
filed this 23<sup>rd</sup> day of February 2007, with:

Docket Control  
ARIZONA CORPORATION COMMISSION  
1200 West Washington  
Phoenix, Arizona 85007

<sup>1</sup> See Rebuttal Testimony of Cindy Liles at pages 20-21 in Docket No. W-01445A-06-0199 et al.

ROSHKA DeWULF & PATTEN, PLC  
ONE ARIZONA CENTER  
400 EAST VAN BUREN STREET - SUITE 800  
PHOENIX, ARIZONA 85004  
TELEPHONE NO 602-256-6100  
FACSIMILE 602-256-6800

1 Copies of the foregoing hand-delivered/mailed  
2 this 23<sup>rd</sup> day of February 2007, to:

3 Chairman Jeff Hatch-Miller  
4 Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

5 Commissioner William A. Mundell  
6 Arizona Corporation Commission  
1200 West Washington Street  
7 Phoenix, Arizona 85007

8 Commissioner Mike Gleason  
9 Arizona Corporation Commission  
1200 West Washington Street  
10 Phoenix, Arizona 85007

11 Commissioner Kristin K. Mayes  
12 Arizona Corporation Commission  
1200 West Washington Street  
13 Phoenix, Arizona 85007

14 Commissioner Gary Pierce  
15 Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

16 Lyn Farmer, Esq.  
17 Chief Administrative Law Judge  
Hearing Division  
18 Arizona Corporation Commission  
1200 West Washington  
19 Phoenix, Arizona 85007

20 Christopher C. Kempley, Esq.  
21 Chief Counsel, Legal Division  
Arizona Corporation Commission  
1200 West Washington  
22 Phoenix, Arizona 85007

23 Ernest G. Johnson, Esq.  
24 Director, Utilities Division  
Arizona Corporation Commission  
1200 West Washington  
25 Phoenix, Arizona 85007

26 By \_\_\_\_\_

27